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C O N F I D E N T I A L SECTION 01 OF 02 SANAA 000966

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TAGS: [EPET](#) [ECON](#) [YM](#) [ECON](#) [COM](#) [ENERGY](#)

SUBJECT: ROYG REJECTS BLOCK 18 EXTENSION: HUNT CONTEMPLATES
"NUCLEAR OPTION"

REF: A. SANAA 326

[B](#). SANAA 04 1537

[C](#). SANAA 106

[D](#). SANAA 196

Classified By: Ambassador Thomas C. Krajewski for reasons 1.5 b and d.

[1](#). (C) Summary. On April 13, Ambassador met with Wyndell Caviness, Vice President and General Manager of Yemen Hunt Oil to discuss the ROYG's rejection of the Block 18 extension. It appears certain that there are no further negotiating options for Hunt and that they have decided to pursue litigation as their only course of action. Caviness was explicit that he did not want Post to advocate on Hunt's behalf. Ambassador made clear that litigation could have a negative effect on bilateral relations and Yemen's often stated intention to attract U.S. and foreign investment. Without the extension, Hunt's future investments in Yemen are in doubt, specifically in liquid natural gas. Protracted litigation could have a disastrous effect on Yemen's economy, and the ROYG's true motives for rejecting the deal remain unclear. End summary.

The End of the Pipeline for Hunt

[2](#). (C) Ambassador met April 13 with Yemen Hunt Vice President and General Manager Wyndell Caviness to discuss deteriorating relations between Hunt Oil and the ROYG. Caviness reviewed Hunt's history in Yemen, which dates back uninterrupted to [1981](#). The meeting followed an April 5 Cabinet Decree supporting Parliament's decision to reject an extension of Hunt's drilling rights in Block 18. Caviness said the move was politically motivated and violated Hunt's legitimate agreement with the Ministry of Oil (MOO), signed in January [2004](#). He added that there was no legal obligation for the ROYG to refer the extension to Parliament, and that Minister of Oil Rasheed Baraba repeatedly claimed authority to ink the deal.

[3](#). (C) There is as yet no official letter from the ROYG to Hunt, but several ROYG insiders stated explicitly that the decision is final and ruled out any intervention from President Saleh. Caviness said that Hunt is left with no choice but litigation. The oil company will likely sue the ROYG in Paris, on the grounds that the agreement with MOO is a legal document signed in good faith. Caviness explained that Hunt cannot afford to set a precedent of capitulation, considering its business interests around the world.

Hunt: "Don't Advocate on our Behalf"

[4](#). (C) Senior ROYG officials, said Caviness, including the MOO and Presidential Advisor Dr. al-Iryani, suggested that USG intervene with Saleh on behalf of Hunt. Caviness rejected this option, and explained that Hunt Oil wanted to avoid any suggestion of improper conduct. Ambassador said this was clear, but that a high profile conflict between the ROYG and a U.S. company could complicate bilateral relations at a critical time. Post will explore this issue from a foreign policy perspective, said Ambassador, as it would have an adverse effect on the ROYG's stated commitment to improving the investment climate as part of the MCC Threshold Program.

Will Oil and Gas Flow From Block 18?

[5](#). (C) The Cabinet decision stated that Block 18 will no longer be operated as a profit sharing operation, but instead be directly owned by the ROYG, which will hire the services of an operator. There are few details on how the government plans to implement this, or who the prospective operators may be. Caviness said ROYG projections of an additional USD one billion income are "a joke." If there is no extension, Hunt will freeze developments in the field, contended Caviness, and many current employees will be forced to seek employment elsewhere. If the case were tied up in court, Caviness continued, both ROYG and Hunt revenue would be locked in escrow pending a decision. Even if the ROYG wins in court, a public dispute with Hunt may deter legitimate companies from

doing business in Yemen.

16. (C) Failure to honor Hunt's Block 18 extension agreement will likely have a negative impact on the ROYG's recent USD 2.5 billion liquid natural gas (LNG) agreements (ref A). Initial LNG production is expected to come from Block 18, and Caviness suggested that extended litigation would delay output. He also hinted that the ROYG is not satisfied with the deal it signed with Kogas (the Korean Gas Company), and may subject the LNG deal to Parliamentary approval as well. In combination with Parliament's rejection of the Block 18 extension, Caviness believes such actions would cause other foreign companies to rethink LNG investments. (Note: Hunt owns 18 percent of the Yemen LNG company. End note.)

Hunt Caught up in the Corruption Debate

17. (C) In an earlier meeting with econoff, former parliamentarian Dr. Saadaldeen Talib shared his view that Parliament acted appropriately in blocking the Hunt extension. According to Talib, the legislature has the legal responsibility to review ROYG contracts with foreign investors, and in the wake of last year's oil scandal would have been negligent not to do so (ref B). The fault did not lie with Hunt, said Talib, but with the MOO for signing an insider deal that would have cost the Yemeni people revenue. The extension agreement included 15 percent profits for CREST, a little known company with ties to corrupt officials. In Talib's view, it was Parliament's role to stamp out corruption and the Cabinet had a moral obligation to comply. Caviness argued that in rejecting the extension Parliament was "throwing the baby out with the bathwater," as Hunt's experience and expertise would result in greater profits from Block 18. He added that Parliament's hasty deliberation on the matter proves that the ROYG was using the GPC-controlled legislature as a convenient excuse for canceling the deal.

Hunt's Departure Bad for Yemen, Bad for US-ROYG Relations

18. (C) Comment: A protracted dispute with Hunt would have a direct negative effect on Yemen's economy. Eighty percent of Yemen's budget is derived from oil profits and, according to Caviness, the Hunt concession accounts for thirty percent of the country's total oil production. Following on the heels of Proctor and Gamble's litigation and withdrawal from Yemen due to IPR disputes, Hunt's departure would cast a large shadow over any future U.S. private investment. Coupled with doubt over the legitimacy of the Aden Port tender, it would be even more difficult for the ROYG to attract much needed foreign direct investment (ref C), a major milestone in Yemen's MCC threshold proposal bid for MCC country status.

19. (C) Comment continued: Understanding the ROYG's motives on the Block 18 extension is an exercise in divination. If Parliament is indeed flexing its muscles in combating corruption, this could be viewed as a positive sign for democratic reform in Yemen. A pattern appears to be emerging, however, in which the ROYG uses the GPC-controlled Parliament to block unpopular decisions (such as economic reforms), blaming democracy for the setback. The decision on Block 18 follows another developing pattern of backdoor nationalization and reverse privatization (ref D). Close advisors to the President, keen on immediate profits and personal gain, are winning the day over reformers who favor an improved investment climate and long-term growth. Considering Hunt's central role in U.S. investment in Yemen, each of these possibilities poses significant challenges to future bilateral relations. Post will keep its eyes and ears open as the case progresses, but will not advocate for Hunt unless specifically asked to intervene. End comment.
Krajeski